

Message Text

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ACTION ARA-10

INFO OCT-01 ISO-00 EB-07 H-02 INR-07 L-02 OES-03 PM-03

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FM AMEMBASSY LIMA

TO SECSTATE WASHDC PRIORITY 5093

C O N F I D E N T I A L SECTION 1 OF 2 LIMA 3858

STADIS////////////////////////////////////

FOR ARA/LA/EP -CORY

EO 11652: GDS

TAGS:: BDIS, ENRG, EINV, EGEN, PFOR, PE

SUBJECT: OCCIDENTAL-PETROPERU IMPASSE THREATENS OXY'S

POSITION AND OVERALL VIABILITY OF TRANS-

ANDEAN PIPELINE PROJECT

REFS: LIMA 3839, LIMA 2546, LIMA 2091, DEPT. MEMCON (OXY-ARA)
OF 4/4/75

1. SUMMARY: A CRITICAL IMPASSE HAS OCCURRED IN CURRENT
NEGOTIATIONS BETWEEN OCCIDENTAL AND PETROPERU OVER OXY'S
FUTURE IN PERU. CONTRARY TO PREVIOUS FIRM COMMITMENT THAT IT WOULD
BUILD PIPELINE, PETROPERU HAS NOW OFFICIALLY NOTIFIED OXY IT
MUST BUILD THE SPUR LINE ITSELF AND HAS SIMULTANEOUSLY NULLIFIED
EARLIER TENTATIVE AGREEMENT FOR ANY OXY THRU-PUT TARIFF FOR USE
OF THE MAIN PIPELINE AT \$1.10 PER BBL. AND IS NOW DEMANDING \$6.81 PER
BBL. EXY MANAGMENT IS PRESENTLY STUDYING SITUATION
AT ITS CALIFORNIA HEADQUARTERS AND HAS SUSPENDED NEW
DRILLING OPERATIONS IN ITS JUNGLE BLOCK AS COUNTER-
MEASURE. LOCAL OXY MANAGER HERE HAS EXPRESSED SERIOUS
CONCERN OVER PETROPERU'S TACTICS AS WELL AS POSSIBILITY
THAT OXY MAY NOT BE ABLE TO OBTAIN NECESSARY FINANCING
FOR ITS SPUR. UNLESS GOP TAKES MORE REASONABLE POSITION
ON T A R F F AND/OR IS ABLE TO COME UP WITH FINANCING,
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AN IMPASSE COULD RESULT WHICH COULD IN TURN JEOPARDIZE

NOT ONLY OXY'S STATUS HERE, BUT OTHER OIL COMPANIES AS WELL, NOT TO MENTION OVERALL ECONOMIC FEASIBILITY OF PIPELINE PROJECT WHICH DEPENDS ON OXY'S OIL TO MAKE IT marginally ECONOMIC.

2. AS IN THE CASE OF THE OVERALL PETROLEUM PICTURE (LIMA 3839), IT IS UNCLEAR WHETHER GOP FULLY UNDERSTANDS SERIOUSNESS OF SITUATION AND APPRECIATES CONSEQUENCES OF ATTEMPTING TO FORCE OXY TO FINANCE ITS LINE WHILE SEEKING TO CHARGE EXORBITANT TARIFF RATE. ALSO UNCLEAR WHETHER THERE HAS BEEN COORDINATED EFFORT, PERHAPS AT MINISTRY OF ENERGY AND MINES LEVEL, TO PUSH OXY INTO A FINANCIAL CORNER. PICTURE COMPLICATED BY FACT THAT OXY PRESIDENT ARMAND HAMMER HAS ALREADY SPENT \$OI MILLION IN EXPLORATION AND DEVELOPMENT AND HAS ALSO PRAISED GOP LAVISHLY, TO POINT THAT GOP HAS PROBABLY TAKEN HIS RHETORIC AT FACE VALUE, THEREBY MAKING IT MORE DIFFICULT FOR OXY TO ENGAGE IN HARD BARGAINING WITH TOUGH GOP NEGOTIATORS.

3. ON SEPARATE BUT RELATED ISSUE, TRANS-ANDEAN PIPELINE LACKS ABOUT \$150 MILLION IN LOCAL CURRENCY FINANCING (OUT OF \$697 MILLION). GOP IS LEANING TOWARD BORROWING DOMESTICALLY TO MEET THIS COST, BUT COULD DECIDE TO GO INTO INTERNATIONAL MARKET TO BORROW MONEY, IN WHICH CASE PETROPERU MIGHT BE INTERESTED IN HAVING EX-IM CONSIDER FINANCING PART A PORTION OF THE \$150 MILLION (PERHAPS \$30-50 MILLION). THIS, HOWEVER, APPEARS INCREASINGLY UNLIKELY. PIPELINE CONSTRUCTION IS ON SCHEDULE, BUT THERE WILL PROBABLY BE SLIPPAGE, AND WE ESTIMATE LINE WILL BE COMPLETED IN EARLY 1977. END SUMMARY.

4. PETROPERU TURNS TABLES ON OXY - DURING LAST SEVERAL WEEKS, WE HAVE RECEIVED SEVERAL INDICATIONS THAT GOP WOULD DECIDE OFFICIALLY TO REQUEST OXY TO BUILD ITS OWN SPUR LINE TO MAIN TRANS-ANDEAN PIPELINE, THUS, REVERSING ITS EARLIER STATED POLICY THAT PETROPERU WOULD BUILD THE SPUR ITSELF. ON MAY 2, LOCAL OXY MANAGER RECEIVED OFFICIAL NOTIFICATION FROM PETROPERU REVOLVING THE PREVIOUS PETROPERU COMMITMENT TO BUILD THE LINE AND INFORMING OXY THAT UNDER ITS CONFIDENTIAL

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CONTRACT IT IS OBLIGED TO BUILD THE LINE. DURING THE SAME WEEK, OXY WAS ALSO NOTIFIED IN MEETING WITH COL. LUNA, NEW ASST. GEN MANAGER OF PETROPERU, THAT PETROPERU WOULD CHARGE OXY \$6.81 PER BBL. AS TARIFF FOR ITS OIL TO BE PUMPED THROUGH PETROPERU'S MAIN PIPELINE, IN CONTRAST TO EARLIER TENTATIVE AGREEMENT WITH OXY FOR A TARIFF OF APPROXIMATELY \$1.10 PER BBL. HEAD OF OXY'S PERUVIAN SUBSIDIARY, DAVID MARTIN, HAS

RETURNED TO CALIFORNIA TO DISCUSS COURSES OF ACTION WITH HIS HEADQUARTERS MANAGEMENT AND IS EXPECTED BACK WITHIN ANOTHER TWO WEEKS. IN THE MEANTIME, AS COUNTER-MEASURE, OXY HAS SUSPENDED SOME DRILLING OPERATIONS AND HAS ONE OF ITS TWO RIGS TEMPORARILY "STACKED", TO THE CONCERN OF PETROPERU.

5. LOCAL OXY MANAGER (U.S. CITIZEN) SPECULATES THAT PETROPERU HAS RECEIVED HARD LINE INSTRUCTIONS FROM MINISTRY OF ENERGY AND MINES AND POSSIBLY DIRECTLY FROM PRESIDENT AND/OR THE CABINET. MANAGER EXPLAINS THAT OXY HAS ALREADY SPENT \$98 MILLION IN PERU AND THAT BEFORE CONTINUING WITH FURTHER MAJOR DRILLING/DEVELOPMENT EFFORTS OXY MUST KNOW WHAT THE TOTAL ECONOMIC FEASIBILITY OF ITS OPERATIONS WILL BE, AND THIS IN TURN DEPENDS IN THE FIRST INSTANCE ON THE TARIFF AGREEMENT. THUS, OXY CANNOT MAKE BASIC DECISIONS ABOUT WHICH WELLS TO DRILL AND EXLPOIT, PENDING RESOLUTION OF THE TARIFF ISSUE. MANAGER DID SAY OXY/PETROPERU ARE NOW BARGING 5,000 B/D FROM OXY'S FIELDS (LAST WEEK'S FIGURES) TO MANAUS, BRAZIL.

6. WILLIAMS BROS. TURN-KEY CONSTRUCTION OF OXY SPUR - MANAGER SAID THAT WILLIAMS BROS./BECHTEL/OXY DISCUSSIONS ABOUT POSSIBILITY OF WILLIAMS OBTAINING CONTRACT FOR CONSTRUCTION OF THE SPUR HAVE ENDED, AND APPARENTLY WILL NOT BEGIN AGAIN UNTIL THRU-PUT ISSUE IS RESOLVED, IF THEN. HE ADDED THAT HE BELIEVES OXY IS HAVING FINANCIAL DIFFICULTIES RAISING THE MONEY, BUT CLAIMED NOT TO BE AWARE OF DETAILS, WHICH DAVE MARTIN IS WORKING ON IN CALIFORNIA. (COMMENT: VISITING U.S. BANKERS HAVE INFORMED US THAT OXY FAILED IN AN ENDEAVOR TO RAISE MONEY FOR THE SPUR THROUGH THE U.S. CONFIDENTIAL

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BOND MARKET AND THAT, FURTHER, EX-IM HAS TOLD OXY THAT IT IS NOT INTERESTED IN FINANCING THE OXY SPUR. WE WOULD APPRECIATE DEPARTMENT'S CHECKING THIS POINT WITH EX-IM AND INFORMING US OF ITS POTENTIAL INTEREST.)

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ACTION ARA-10

INFO OCT-01 ISO-00 EB-07 H-02 INR-07 L-02 OES-03 PM-03

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P 121530Z MAY 75

FM AMEMBASSY LIMA

TO SECSTATE WASHDC PRIORITY 5094

C O N F I D E N T I A L SECTION 2 OF 2 LIMA 3858

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7. OXY'S RESERVES "AN EMPTY PIPELINE" - ACCORDING TO LOCAL OXY MANAGER, LATEST DEGOLYER & MCNAUGHTON STUDY STATES THAT OXY HAS 198 MILLION BBLs. OF PROVED RESERVES. THIS FIGURE DOES NOT INCLUDE LATEST OXY FINDS AS IS SAME FIGURE EMBASSY RECEIVED CONFIDENTIALLY FROM WELLS FARGO REPRESENTATIVES WHO HAD ACCESS TO THE DEGOLYER AND MCNAUGHTON STUDY. ALTHOUGH FIGURES ON PETROPERU'S FIELDS HAVE NEVER BEEN AVAILABLE TO US ON THE BASIS OF DISCUSSIONS WITH NUMEROUS SOURCES WE ESTIMATE THAT PETROPERU MIGHT HAVE 80-100 MILLION BBLs. (PUBLICALLY, GOP CLAIMS PETROPERU HAS OVER 200 MILLION BBLs AND PRIVATELY HAS TOLD US IT HAS OVER 300 MILLION BBLs.) OF PROVEN RESERVES. THUS, OXY'S ROLE IN FILLING THE MAIN PIPELINE IS CRUCIAL TO THE SUCCESSFUL OPERATION OF THE LINE. BASED ON PUBLIC ANNOUNCEMENTS AND OXY AND PETROPERU SOURCES, WE PRESUME OXY CAN PUMP 50-60,000 B/D INITIALLY, WITH PETROPERU PUMPING 20-30,000 B/D. (PUBLICALLY, PETROPERU HAS CLAIMED IT CAN INITIALLY PUMP OVER 60,000 B/D.) OUR FIGURE IS JUST ENOUGH TO JUSTIFY THE PIPELINE AT CURRENT RATE OF CONSUMPTION (40,000 B/D DEFICIT), PLUS 50,000 B/D PAY-BACK TO THE JAPANESE. HOWEVER, AS LOCAL MANAGER NOTED, IT IS NOW TOO LATE TO BUILD OXY SPUR FOR COMPLETION AT SAME TIME AS MAIN-LINE, SO THAT INITIALLY THE MAIN-LINE MAY TAKE SEVERAL MONTHS TO FILL (USING PETROPERU'S OIL ALONE, AFTER SO MUCH FANFARE, CONFIDENTIAL

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THESE MEAGRE RESULTS WILL PROVE EMBARRASSING TO GOP.

8. FINANCING OF TRANS-ANDEAN PIPELINE - COFIDE OFFICIALS HAVE ASSURED US THAT MOST OF FINANCING FOR THE PIPE-

LINE HAS BEEN ACQUIRED, BUT HAVE NOTED THERE IS A \$150 MILLION PORTION FOR LOCAL COSTS STILL LACKING. THEY SAY THAT PRIME MINISTER MORALES BERMUDEZ WILL MAKE A DECISION SHORTLY ABOUT WHETHER TO INCREASE THE INTERNAL GOVERNMENT DEBT BY BORROWING FROM THE PERUVIAN TREASURY, OR BY GOING ON THE INTERNATIONAL MARKET TO RAISE THE MONEY IN FOREIGN CURRENCY FOR CONVERSION INTO SOLES. PETROPERU PRESIDENT FERNANDEZ BACA TOLD THE AMBASSADOR RECENTLY THE GOP WOULD OPT FOR THE FORMER SOLUTION. COFIDE NOTES THAT IF THE SECOND APPROACH IS USED, THEN COFIDE MAY BE INTERESTED IN HAVING SOME EX-IM PARTICIPATION, IF POSSIBLE. IN ANY CASE, TO DATE NO CONCRETE INFORMATION ABOUT THE FEASIBILITY OF THE PIPELINE HAS BEEN MADE AVAILABLE TO US FOR TRANSMISSION TO EX-IM, AND WE DO NOT EXPECT TO RECEIVE SUCH INFORMATION SOON IF AT ALL. A REQUEST FOR EX-IM PARTICIPATION IN THE MAIN PIPELINE IS THEREFORE UNLIKELY.

9. COMMENT: OXY MANAGEMENT HERE PRESUMES (AND WE AGREE) THAT SEVERAL FACTORS HAVE PROBABLY CONTRIBUTED TO DECISION BY GOP TO MAKE OXY BUILD FEEDER AND CHARGE HIGH (AND UNECONOMIC) RATE FOR THRU-PUT OF ITS OIL. FIRST, FACT THAT OXY HAS ALREADY INVESTED CLOSE TO \$100 MILLION AND HAS POTENTIALLY COMMERCIALY VIABLE FIELD; SECOND, HAMMER'S PUBLIC AND PRIVATE STATEMENTS ABOUT STRENGTH OF HIS COMPANY AND ITS SUPPORT FOR PERUVIAN REVOLUTION; THIRD, DETERIORATING BALANCE OF PAYMENTS POSITION AND FACT THAT GOP DOES NOT WISH TO ASSUME ADDITIONAL DEBT BURDEN AT THIS TIME BUT WISHES TO SHIFT IT TO COMPANY; FOURTH, DIVISION OF RESPONSIBILITY FOR DECISIONS BETWEEN PETROPERU (WITH TECHNICAL EXPERTISE AND KNOWLEDGE) AND MINISTRY OF ENERGY AND MINES, LED BY HIGHLY POLITICAL AND RADICAL JORGE FERNANDEZ MALDONADO, WHO POSSIBLY PERCEIVES OCCIDENTAL AS A LIKELY TARGET WITH WHICH TO PROVE HIS REVOLUTIONARY

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CREDENTIALS. THE SITUATION IS NOT YET DEADLOCKED, HOWEVER, AND WE THINK IT LIKELY THAT OCCIDENTAL AND PETROPERU MAY EVENTUALLY BE ABLE TO REACH A VIABLE COMPROMISE ON THE TRARIFF COST. (ON THIS SUBJECT, A PETROPERU OFFICIAL LET SLIP TO AN EMBASSY OFFICER A FEW WEEKS AGO THAT HE THOUGHT FINAL AGREEMENT COULD BE REACHED AT \$3-4 PER BBL.) OCCIDENTAL ALSO HAS THE OPTION, PRESUMABLY BEING CONSIDERED AT ITS HEADQUARTERS, OF SLOWING DOWN ITS DRILLING AND DEVELOPMENT PROGRAM AND USING SOME OF THE MONEY THEREBY FREED FOR THE CONSTRUCTION OF THE SPUR LINE. THIS WOULD, OF COURSE, CONSIDERABLY REDUCE THE INITIAL OIL

PRODUCTION FIGURES FOR THE MAIN PIPELINE, BUT IS ONE
POSSIBILITY. FURTHER, IF OXY CAN MAKE A CASE THAT IT
CANNOT RAISE SUFFICIENT FUNDS TO FINANCE THE
LINE, IT IS POSSIBLE
THAT THE GOP WHEN FACED WITH THE EMBARRASSING CON-
SEQUENCES MENTIONED ABOVE MIGHT ULTIMATELY DECIDE TO
BUILD THE LINE ITSELF.
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Message Attributes

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